

China / Hong Kong Company Update

AIA Group

Bloomberg: 1299 HK Equity | Reuters: 1299.HK

Refer to important disclosures at the end of this report

DBS Group Research . Equity

26 Aug 2020

BUY

Last Traded Price (26 Aug 2020): HK\$77.8 (HSI : 25,486)
Price Target 12-mth: HK\$92.00 (18% upside) (Prev HK\$90.00)

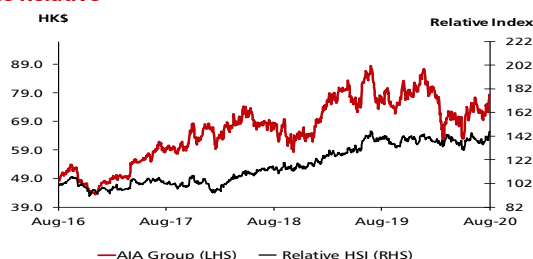
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What's New

- AIA China contributed 38% of total VONB in 1H20 and outpaced AIA HK's contribution for the first time
- Additional VONB contribution from China's market liberalisation to reach US\$2.6bn by FY26F
- Lower VONB forecasts by 15% for FY20/21F on COVID-19 impact, but revise up AIA China's VONB growth by 6-8%
- Roll over valuation base to FY21F, and revised up TP to HK\$92, based on our two-stage EV growth model

Price Relative



Forecasts and Valuation

FY Dec (US\$ m)	2018A	2019A	2020F	2021F
Net earned premiums	29,716	32,896	34,384	37,734
Net investment income	8,076	8,899	9,538	10,531
Net Profit	5,298	5,749	6,052	6,853
EPS (US\$)	0.22	0.55	0.43	0.65
EPS (HK\$)	1.68	4.28	3.37	5.08
EPS Gth (%)	(59.8)	154.2	(21.3)	50.6
PE (X)	46.2	18.2	23.1	15.3
DPS (HK\$)	1.13	1.26	1.32	1.50
Net Div Yield (%)	1.5	1.6	1.7	1.9
BV Per Share (HK\$)	25.03	36.91	38.94	42.50
P/Book Value (X)	3.1	2.1	2.0	1.8
P/EV (X)	2.2	2.0	1.9	1.7
ROAE (%)	6.4	13.8	8.9	12.4

Earnings Rev (%): 2 1
Consensus EPS (US\$) 0.43 0.58
Other Broker Recs: B: 24 S: 1 H: 2

Source of all data on this page: Company, DBS Bank (Hong Kong) Limited ("DBS HK"), Thomson Reuters

Embracing the next expansion cycle

Investment Thesis

Contribution from China to accelerate. AIA China's VONB contribution has outpaced AIA HK's for the first time and reached 38% in 1H20. Growth is expected to start accelerating from hereon.

Well-positioned for the next expansion. Targeting 12 new provinces/municipalities by FY30F with an addressable market 4x larger than the current footprint offers a grand opportunity.

VONB to double by FY25F. Additional VONB contribution from China expansion is estimated to result in the doubling in VONB by FY25F.

Valuation:

Our TP is based on a two-stage EV growth model, with a) first stage to factor in existing organic growth, and b) second stage to include the present value (PV) of additional VONB from China due to market liberalisation, and is pegged to a 2.0x FY21 P/EV multiple.

Where we differ:

Most of the consensus moderately revised down AIA's TP due to the weak overall VONB growth in 1H20. However, the market has neglected the better-than-expected growth outlook from AIA China which we believe should be the main share price driver.

Key Risks to Our View:

Slower VONB growth, sharp deterioration of investment performance, slower economic growth in China.

At A Glance

Issued Capital (m shrs)	12,089
Mkt Cap (HK\$/US\$m)	941,733 / 121,508
Major Shareholders (%)	
Capital Research Global Investors	7.4
Free Float (%)	92.6
3m Avg. Daily Val. (US\$m)	272.55
GLCS Industry: Financials / Insurance	



Live more, Bank less

WHAT'S NEW

Embracing the next expansion cycle

Disappointing 1H20 VONB results but negatives priced in

Impacted by the current pandemic, AIA reported weaker-than-expected VONB (value of new business) growth in 1H20, which fell 37% y-o-y. The main drag came from the Hong Kong market, where the lockdown measures had prevented inbound travel of Mainland China visitors. Along with the change in product mix by shifting to lower-margin and deferred annuities products, this has resulted in a 68%/59% y-o-y decline in VONB/ANP (annual new premium), respectively. For other major markets, AIA Thailand, AIA Singapore, and AIA Malaysia also posted a 7%/24%/36% y-o-y decline in VONB, respectively. However, with growth in 2Q20 starting to see sequential improvement, we believe the negatives have been priced in.

AIA China performance surprised on the upside

On the other hand, AIA China posted better-than-expected results, with ANP posted flat y-o-y and VONB posted down only 13% y-o-y. VONB margin contracted to 81.8% (down 11.5 ppts) mainly on product mix shift in long-term participating saving products. Backed by its strong digital capabilities which enable AIA to timely resume normal business operations once the lockdown measures are gradually relaxed, AIA China managed to post positive VONB growth in 2Q, and this momentum also continued into July. With China's economic activities gradually returning to normal, we expect to see a strong growth recovery in 2H20F, and now forecast AIA China's VONB/ANP to post +3%/+15% y-o-y in FY20F, versus our previous forecast of each down 5% y-o-y.

Marching ahead

On June 2020, AIA China received approval from CBIRC to convert its Shanghai branch into a wholly-owned subsidiary, and will start the application process for regulatory approvals to establish new branches outside its existing five geographic territories. We believe this marks a new era for AIA, and the ability to expand outside its existing five geographical territories in China offers a huge long-term growth opportunity for the insurers.

According to the management, AIA China will focus on 12 new provinces/municipalities in the next 10-year expansion plan in China, which will offer more than 4x of the addressable market as compared to its existing footage. While

management has yet to offer details of the future China expansion plan, if we refer to its successful and proven record from AIA Jiangsu (nine cities post Suzhou and Nanjing) growth trajectory where the VONB growth has recorded a 67% CAGR within six years of its debut (AIA Jiangsu was established in 2013), we believe its future VONB growth opportunity in China is phenomenal. We also see its premium agency strategy, strong digital enablement and high-quality management will serve as a solid foundation for future success.

VONB to double by FY25F

Assuming 1) AIA China to expand into one new territory per year, 2) an 8% p.a. headcount growth from existing footprints, 3) agent from new territory takes five years for its productivity to be in line with existing agents, 4) a 10% p.a. agent productivity growth from existing territories, and 5) refer a 9.75% discount rate, in line with the discount rate AIA current refers to its China business. Our estimate suggests that the present value of the additional VONB generated from new territory expansion in China may reach US\$1.8bn by FY26F, which is equivalent to 1.5x of our estimated AIA China VONB in FY20F, or 53% of our estimated AIA total VONB. The additional VONB generated will also enable AIA to double its VONB in the next 5-years (figure 1).

Lift TP to HK\$92 based on our 2-stage EV growth model

As impacted by the current pandemic, we lower AIA's VONB forecast by 15% each in FY20/21F, mainly to factor in the weaker-than-expected growth outlook from AIA Hong Kong. On the other hand, we revised up AIA China's VONB forecast by 6-8% for FY20-FY21F, on the back of the better outlook. By rolling our valuation base to FY21F and based on our 2-stage EV growth model where we estimate the China business expansion to generate an additional 3% value to FY21F EV and refer a 2.0x P/EV multiple (2.1x previously). We derive a new TP of HK\$92 (compared to HK\$90 previously, see figure 2). With 18% potential upside, we reiterate our BUY call on AIA.

Fig 1: Estimation of AIA China's VONB growth by FY26F

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020F	2021F	2022F	2023F	2024F	2025F	2026F
Existing footprint															
TWPI (US\$m)	1,446	1,599	1,786	2,028	2,383	3,118	4,006	4,804	5,920	7,140	8,143	9,485	11,052	12,882	15,021
ANP (US\$m)	215	249	311	438	621	873	1,067	1,248	1,435	1,716	2,039	2,422	2,877	3,418	4,061
YoY (%)		16%	25%	41%	42%	41%	22%	17%	15%	20%	19%	19%	19%	19%	19%
VNB (US\$m)	124	166	258	366	536	725	965	1,167	1,199	1,467	1,764	2,119	2,532	3,025	3,614
YoY (%)		34%	55%	42%	46%	35%	33%	21%	3%	22%	20%	20%	19%	19%	19%
VNB margin (%)	58%	67%	83%	84%	86%	83%	90%	94%	84%	86%	87%	88%	88%	89%	89%
No. of agent ('000)			15				39	43	44	46	50	54	59	63	68
YoY (%)								10%	2%	6%	8%	8%	8%	8%	8%
Agent productivity (US\$'000)							27	29	33	37	41	45	49	54	59
YoY (%)								6%	13%	13%	10%	10%	10%	10%	10%
New expansion area - 1															
No. of agent ('000)										1	2	3	5	6	8
YoY (%)											100%	60%	50%	35%	30%
Agent productivity (US\$'000)										30	35	40	47	54	59
ANP (US\$m)										30	69	129	224	350	501
VNB margin (%)										86%	87%	88%	88%	89%	89%
VNB (US\$m)										25	60	113	197	310	446
New expansion area - 2															
No. of agent ('000)											1	2	3	5	6
YoY (%)											0%	100%	60%	50%	35%
Agent productivity (US\$'000)											30	35	40	47	54
ANP (US\$m)											30	69	129	224	350
VNB margin (%)											86%	87%	88%	88%	89%
VNB (US\$m)											25	60	113	197	310
New expansion area - 3															
No. of agent ('000)												1	2	3	5
YoY (%)												0%	100%	60%	50%
Agent productivity (US\$'000)												30	35	40	47
ANP (US\$m)												30	69	129	224
VNB margin (%)												86%	87%	88%	88%
VNB (US\$m)												25	60	113	197
New expansion area - 4															
No. of agent ('000)													1	2	3
YoY (%)													0%	100%	60%
Agent productivity (US\$'000)													30	35	40
ANP (US\$m)													30	69	129
VNB margin (%)													86%	87%	88%
VNB (US\$m)													25	60	113
New expansion area - 5															
No. of agent ('000)														1	2
YoY (%)														0%	100%
Agent productivity (US\$'000)														30	35
ANP (US\$m)														30	69
VNB margin (%)														86%	87%
VNB (US\$m)														25	60
New expansion area - 6															
No. of agent ('000)															1
YoY (%)															
Agent productivity (US\$'000)															30
ANP (US\$m)															30
VNB margin (%)															86%
VNB (US\$m)															25
Aggregate VNB (US\$m)	124	166	258	366	536	725	965	1,167	1,199	1,493	1,848	2,317	2,927	3,730	4,765
YoY (%)		34%	55%	42%	46%	35%	33%	21%	3%	25%	24%	25%	26%	27%	28%
Additional VNB generated (US\$m)									-	25	85	198	395	705	1,150

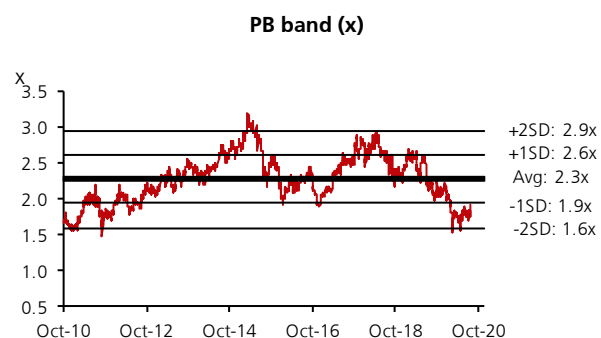
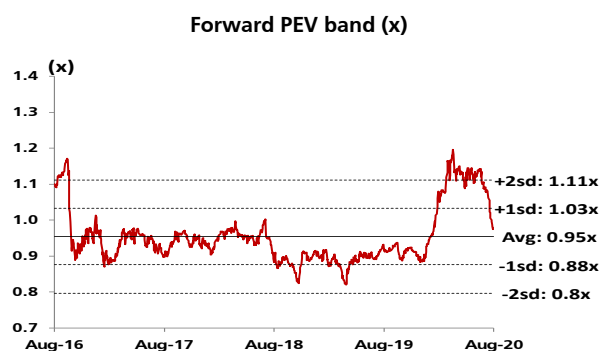
Source: DBS HK

Fig 2: DBS 2-stage EV growth model and AIA target price

USD (mil)	FY17	FY18F	FY19F	FY20F	FY21F
VONB	3,206	3,955	4,186	3,369	3,989
VONB growth		23%	6%	-20%	18%
VIF	29,805	29,880	33,744	33,765	35,063
ANW	20,974	24,637	28,241	30,791	35,252
EV	50,779	54,517	61,985	64,556	70,315
EV growth	0	7%	14%	4%	9%
PV of additional VONB from China expansion (by FY26F)					1,773
Adjusted EV					72,088
No. of shares	12,074	12,074	12,074	12,074	12,074
USD / HKD					7.8
EV per share (HKD)	32.9	35.3	40.1	41.8	46.7
Multiple (x)	0	0	0	0	2.0x
Target price	0	0	0		92.00

Source: DBS HK

Historical PEV and PB band



Source: Bloomberg Finance L.P. DBS HK

Key Assumptions

FY Dec	2017A	2018A	2019A	2020F	2021F
Total weighted premium growth	N/A	15.7	11.3	8.3	9.8
VNB growth	0.0	23.4	5.8	(19.5)	18.4
VNB margin	57.0	60.8	63.6	57.1	58.8
Net investment return	4.8	4.8	4.6	4.0	4.0
Total investment return	8.5	4.8	4.6	4.0	4.0
EV growth	19.0	7.4	13.7	4.1	8.9
Solvency ratio	446.1	420.6	362.3	386.8	389.0

Source: Company, DBS HK

Income Statement (US\$ m)

FY Dec	2017A	2018A	2019A	2020F	2021F
Total weighted premium income	26,393	30,543	34,002	36,814	40,426
Gross written premiums	0	0	0	0	0
Net earned premium	25,941	29,716	32,896	34,384	37,734
Investment income	7,189	8,076	8,899	9,538	10,531
Other operating income	0	0	0	0	0
Total income	33,130	37,792	41,795	43,923	48,265
Benefits and claims	(21,646)	(24,931)	(27,624)	(29,059)	(31,841)
Underwriting and policy acquisition costs	(3,443)	(3,778)	(4,297)	(4,470)	(4,891)
Finance cost	(400)	(475)	(582)	(596)	(618)
Other expenses	(2,036)	(2,171)	(2,468)	(2,700)	(2,884)
Total expenses	(27,525)	(31,355)	(34,971)	(36,825)	(40,233)
Share of profit of associated and JVs	0	0	0	0	0
Profit before tax	5,605	6,437	6,824	7,097	8,032
Income tax expense	(917)	(1,094)	(1,030)	(1,000)	(1,133)
Minority interest	(35)	(45)	(45)	(45)	(45)
Preferred dividend	0	0	0	N/A	N/A
Net income attributable to shareholders	4,635	5,298	5,749	6,052	6,853

Source: Company, DBS HK

Balance Sheet(US\$ m)

FY Dec	2017A	2018A	2019A	2020F	2021F
Total Investment	162,686	171,339	212,776	226,352	242,874
Property, plant and equipment	1,225	1,233	2,865	2,865	2,865
Other assets	54,735	57,234	68,491	73,880	80,438
Total assets	218,646	229,806	284,132	303,097	326,177
Net life reserves - traditional	151,475	164,764	189,597	205,343	222,827
Net life reserves - investment contracts	8,210	7,885	12,273	12,273	12,273
Other Liabilities	15,405	17,751	24,306	24,306	24,306
Total liabilities	175,090	190,400	226,176	241,922	259,406
Shareholder's equity	43,176	39,006	57,508	60,681	66,233
Minority interest	380	400	448	493	538
Total equity	43,556	39,406	57,956	61,174	66,771

Source: Company, DBS HK

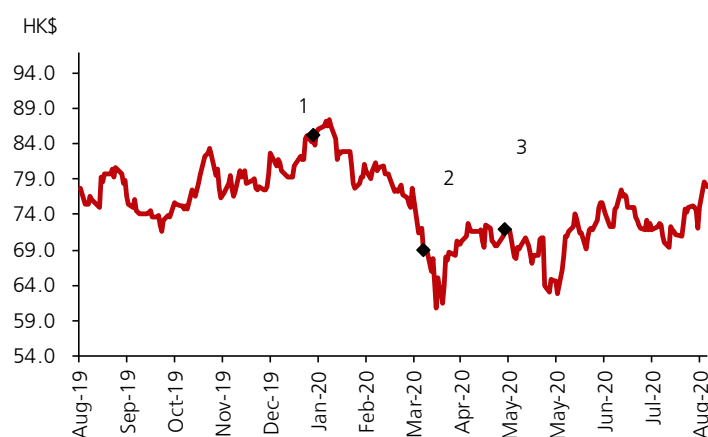
AIA Group

Key Financials & Ratios

FY Dec	2017A	2018A	2019A	2020F	2021F
Du Pont analysis (%)					
Net profit / premium income	25.0	10.1	20.2	15.2	20.9
Premium income / total asset	11.9	12.9	11.6	11.3	11.6
Total asset / total equity	5	6	5	5	5
Return on equity	7.9	6.4	13.8	8.9	12.4
Embedded value(US\$ m)					
Book value	43,176	39,006	57,508	60,681	66,233
Adjusted items	(22,202)	(14,369)	(29,267)	(29,890)	(30,981)
Adjusted book value	20,974	24,637	28,241	30,791	35,252
Value-in-force	29,805	29,880	33,744	33,765	35,063
Group embedded value	50,779	54,517	61,985	64,556	70,315
Per share analysis(US\$)					
EPS	0.54	0.22	0.55	0.43	0.65
BPS	3.58	3.23	4.76	5.02	5.48
DPS	0.13	0.15	0.16	0.17	0.19
EVPS	4.21	4.51	5.13	5.35	5.82
Capital Strength (%)					
Leverage ratio	0	0	0	0	0
Solvency ratio	446.1	420.6	362.3	386.8	389.0

Source: Company, DBS HK

Target Price & Ratings History



S.No.	Date	Closing Price	12-mth Target Price	Rating
1:	7-Jan-20	HK\$84.30	HK\$102.00	Buy
2:	12-Mar-20	HK\$68.80	HK\$102.00	Buy
3:	28-Apr-20	HK\$70.95	HK\$90.00	Buy

Source: DBS HK

Analyst: Ken SHIH

Cindy WANG

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STRONG BUY (>20% total return over the next 3 months, with identifiable share price catalysts within this time frame)

BUY (>15% total return over the next 12 months for small caps, >10% for large caps)

HOLD (-10% to +15% total return over the next 12 months for small caps, -10% to +10% for large caps)

FULLY VALUED (negative total return, i.e., > -10% over the next 12 months)

SELL (negative total return of > -20% over the next 3 months, with identifiable share price catalysts within this time frame)

*Share price appreciation + dividends

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Sources for all charts and tables are DBS HK unless otherwise specified.

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